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Supreme Court of the United States

..... Term

No. 197

PHILIP SMOLOWE and M. WILLIAM LEVY, suing on behalf of themselves and as stockholders and for the benefit of all other stockholders of DELENDO CORPORATION similarly situated who may elect to come in and contribute to this action,

Respondents-Appellees,

against

DELENDO CORPORATION (formerly OLDE-TYME DISTILLERS CORPORATION), I. J. SESKIS and HENRY C. KAPLAN,

Defendants-Appellants.

UNITED STATES OF AMERICA,

Intervenor-Appellee.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF.

JAY LEO ROTHSCHILD,
Solicitor for Petitioners.

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PETITION.

TO THE HONORABLE, THE CHIEF JUSTICE OF THE UNITED STATES AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioners respectfully show:

This is a petition for certiorari to review a decree of the United States Circuit Court of Appeals for the Second Circuit (R., p. 146), which affirmed a judgment of the

United States District Court for the Southern District of New York, which said judgment of the District Court adjudged that the defendant Delendo Corporation recover from the defendant Seskis, $9,733.80, and from the defendant Kaplan $9,161.05, with costs as taxed, and further adjudged that the defendant, Delendo Corporation, pay to the attorneys for the plaintiffs $3,078.98, for counsel fees and disbursements (R., pp. 120, 121).

Summary of the Matter Involved.

This is a derivative action, purporting to be brought by plaintiffs, who are stockholders of Delendo Corporation (formerly known as Oldetyme Distillers Corporation), pursuant to the provisions of § 16(b) of the Securities Exchange Act of 1934 (15 U. S. C. A. § 78p(b)), which, in substance, provides that, "For the purpose of preventing the unfair use of information which may have been obtained" by a beneficial owner, director or officer, "by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, * * * shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. * * *"

The action purports to be brought in behalf of said Delendo Corporation against its president and vice-president (the defendants Seskis and Kaplan, respectively), who are also two of Delendo Corporation's directors.

The United States, by reason of the constitutional questions raised, was permitted to intervene pursuant to 28 U. S. C. A. 401.

In the District Court, the case was tried by BRIGHT, *D. J.*, who rendered a judgment, in favor of the corporation, as above stated.

The judgment of the District Court was unanimously affirmed by the Circuit Court of Appeals for the Second Circuit (SWAN, CHASE and CLARK—Circuit Judges; opinion by Judge CLARK).

The judgment was predicated on a finding that the individual defendants had "realized" a "profit" from sales and purchases of the corporation's stock, within a period of six months. But there was also an express and explicit finding that both the defendants, Seskis and Kaplan, had acted in good faith, had not unfairly used any "inside" information, and had not committed any act in violation of their fiduciary obligations to the corporation. Indeed, there was no issue as to these aspects of the case, because the good faith of the defendants was stipulated (fols. 365, 133, 187).

Basis of Jurisdiction.

This court has jurisdiction, upon appeal, to review the judgment or decree in question, for these reasons all predicated upon contentions duly made and appropriately reflected in the record (cf. Answer, fols. 24-33, 59-69, 83-92, 95-98, 117):

(a) The statutory provision which is believed to sustain the jurisdiction of this court, is § 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (28 U. S. C. A. 347).

(b) There is involved both the construction and the validity of a statute of the United States, summarized in the preceding section and set out at page 10 of the annexed brief—known as § 16(b) of the Securities and Exchange Act of 1934, and otherwise known as 15 U. S. C. A. § 78p(b).

(c) The date of the decree of the Circuit Court of Appeals, sought to be reviewed, is June 25, 1943.

(d) The questions presented are (1) as to the construction of the statute in its various phases—more specifically set out in the annexed brief—and (2) as to the validity of the statute under the Fifth Amendment to the Constitution of the United States—relating to due process; under § 1 of Article I and

Paragraph 18 of § 8 of Article I of the Constitution of the United States—relating to delegation of legislative power; and under Clause 3 of § 8 of Article I of, and the Tenth Amendment to, the Constitution of the United States—relating to interstate commerce.

The Questions Presented.

The questions presented are as follows:

A.

As to Construction.

1. Did the Congress intend to exclude consideration of the undisputed fact that inside information was not used by the defendants or either of them, and, therefore, to make liability absolute, irrespective of the fact that there was not any use of inside information?

2. In any event, when the Congress provided that "profit realized" should be recoverable, did it intend, as a condition precedent to liability, that it should be demonstrated that there was an actual profit— on the basis of a comparison of sales and purchases, or purchases and sales of the same stock, according to the rules applicable in computing income taxes—or, on the contrary, did it intend that a profit should be deemed demonstrated to have been made, by matching off purchases at the lowest prices against sales at the highest prices, during the six-months period?

3. In any event, does the Congressional enactment have any application to transactions, the purchase phases of which antedated the effective date of the statute?

4. It being conceded that the defendant Kaplan's receipt of 15,800 shares, in payment of an antecedent indebtedness owing to him from the defendant Seskis, is not within the statute, should not defendant Seskis' delivery of the very same shares, in liquidation of said indebtedness, be deemed beyond the operation of the statute too?

B.

As to Constitutional Validity.

5. Does the Congressional enactment, as construed by the courts below, deprive defendants of property without due process of law, in violation of the Fifth Amendment to the Constitution of the United States,

(a) because it creates a conclusive presumption which penalizes the defendants, without opportunity on their part to be heard to show (and thus became decisive in the consideration of the case) that at no time and in no manner did they use inside information;

(b) because it discriminatorily deprives the defendant Seskis, in any event, of the use value of the stock acquired by him prior to the effective date of the statute, and, therefore, interferes with his vested property rights;

(c) because it fails to take into account whether the shares of stock acquired prior to the six-months period were the shares of stock sold in the six-months period, so that profits are computed on the basis of stock acquired within the six-months period, which was not sold during the six-months period;

(d) because it deprives the defendant Kaplan of alleged but in fact nonexisting profits resulting from the purchase and sale of the same stock within the six-months period, and thus takes his property without due process of law, and constitutes an unreasonable restraint upon his right to use said property;

(e) because the fixation of a period of six months —within which alleged profits made from sales and purchases of stock are appropriated to the corporation—is arbitrary and unreasonable?

6. Does the Congressional enactment, as construed by the courts below, constitute an unauthorized delegation of legislative power to the Securities and Exchange Commission, in violation of §1 of Article I and Paragraph 18 of § 8 of Article I of the Constitution of the United States? In this connection, is not Rule X-16B-1 of the General Rules

and Regulations of the Securities and Exchange Commission—exempting purchases or sales accomplished before the effective date of the statute (i. e., October 1, 1934), providing they were followed, within six months thereafter, by a complementary sale or purchase—both discriminatory and an exercise of legislative power, as applied to complementary phases, in the case at bar, which were executed at a time later than six months after the enactment of the statute?

7. Does the Congressional enactment, as construed by the courts below, constitute an unauthorized invasion into transactions which are not a part of interstate commerce, as contemplated by Clause 3 of § 8 of Article I of, and the Tenth Amendment to, the Constitution of the United States?

C.

As to Fees.

8. Under the Congressional enactment involved, was the District Court authorized to allow counsel fees, in the face of a conclusive showing that there was and could be not the slightest benefit to the corporation, but, on the contrary, a definite disservice and detriment—as a result of the commencement and prosecution of this action—interfering with the dissolution of the corporation, and of no substantial value either to the corporation or its stockholders?

Reasons Relied On For Allowance Of the Writ.

This is the first case arising under and construing § 16(b) of the Securities and Exchange Act of 1934.

The controversy presents an important question of federal law, as well as a question of general importance, which has not been but should be settled by this court—which question has been decided, as we view it, in conflict with applicable decisions of this court, and presents an issue of substance, relating to the construction and applica-

tion of the Constitution of the United States, and which has not been but should be settled by this court—all within the precise contemplation of Subdivisions (b) and (c) of Rule 38 of the Rules of this court.

WHEREFORE, your petitioner prays that a writ of certiorari issue under the seal of this court, directed to the United States Circuit Court of Appeals for the Second Circuit, commanding said Court to certify and send to this Court a full and complete transcript of the record and of the proceedings of the said Circuit Court of Appeals, had in this case, to the end that this cause may be reviewed and determined by this court, as provided for by the statutes of the United States; and that the decree herein of said Circuit Court of Appeals be reversed by this court; and for such other and further relief as to this court may seem proper.

Dated, July 14, 1943.

JAY LEO ROTHSCHILD,
Solicitor for Petitioners.

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(C) Insofar as the statute discriminatorily fails to take into account whether the shares of stock acquired prior to the six-months period, were the shares of stock sold in the six-months period—so that profits are computed on the basis of stock acquired within the six-months period, which was not sold during the six-months period—it also deprives the defendants of vested rights, without due process of law 62

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